

DEPARTMENTAL REGULATION		Number: DR 1110-2
SUBJECT: Management Accountability and Control	DATE: Feb. 23, 1999	
	OPI: Office of the Chief Financial Officer	

1 PURPOSE AND SCOPE

This regulation establishes department wide policy for all agencies and staff offices to improve the accountability and effectiveness of USDA's programs and operations through the use of sound systems of internal and management controls. The intent of the policy contained in this regulation is to ensure that programs are managed with integrity and that program operations comply with applicable laws and regulations. As indicated in OMB Circular A-127, Financial Management Systems, the internal controls associated with financial system inputs, processing, and outputs form a portion of the management control structure required by OMB Circular A-123, Management Accountability and Control.

2 CANCELLATION/SPECIAL INSTRUCTIONS

- a This regulation cancels Department Regulation 1110-2, Internal/Management Controls, issued September 28, 1990.
- b The guidance contained in this regulation supplements and reinforces the statutory requirements of the Federal Managers' Financial Integrity Act of 1982 (FMFIA) and the policy guidance contained in OMB Circular A-123, which pertains to all federal managers.

3 BACKGROUND/AUTHORITY

a FMFIA, Pub. L. No. 97-255, requires agencies to develop cost-effective internal accounting and administrative controls to ensure that federal programs are operated efficiently, effectively, and in compliance with relevant laws. Each year, the Secretary of Agriculture is required to prepare a statement on whether USDA's systems of internal control comply with standards prescribed by the Comptroller General and whether such systems provide reasonable assurance that the following objectives are met:

1. obligations and costs comply with applicable law;
2. funds, property, and other assets are safeguarded against waste, loss, or mismanagement; and
3. revenues and expenditures are properly recorded and accounted for to permit the preparation of reliable financial and statistical reports and to maintain accountability over the assets.

b The law requires the Secretary to include a separate statement on whether USDA's accounting systems conform with certain standards, principles, and other specifications to ensure that federal managers have timely, relevant, and consistent financial information for decision-making purposes. For any material deficiency which is identified during the reporting period, a corrective action plan and schedule for correcting any deficiency must be included in the annual statement.

c OMB Circular A-123 provides guidelines for improving the accountability and effectiveness of Federal programs and operations by establishing, assessing, correcting, and reporting on management controls. OMB Circular A-127 prescribes policies and standards to ensure that Federal financial systems provide complete, timely, reliable, and consistent information to support decision-making.

4 RESPONSIBILITIES

a All Sub-Cabinet Officials, Agency Heads and Heads of Staff Offices within USDA will:

1. Take systematic and proactive actions to implement appropriate, cost-effective internal and management controls for all processes which support the delivery of agency programs and operations.
2. Ensure that internal and management controls for processes supporting agency programs and operations are commensurate

with program risks, results-oriented management, and support the objectives outlined in the above section.

3. Ensure that internal and management controls are an integral part of each organization's entire cycle of planning, budgeting, program delivery or operations, accounting, and auditing processes.
4. Ensure that clear documentation for transactions, internal and management controls and other significant events is readily available for examination.
5. Assess the risks and external factors which may impair program delivery and operations on an annual basis or more frequently, if needed.
6. Commensurate with the level of risk, periodically assess the adequacy of internal and management controls for their respective programs and operations and document results.
7. Identify significant weaknesses in internal and management controls and develop corrective action plans for material deficiencies.
8. Disclose material internal and management control weaknesses to the next level of management.
9. Ensure that the agency strategic or annual performance plans address the correction of material deficiencies identified or disclosed.
10. Ensure that all material deficiencies and significant deficiencies, which are not deemed material to the Department, are corrected in a timely manner.
11. Ensure that all managers and employees are aware of the importance of internal and management controls as well as specific program risks, control objectives, and control measures.
12. Designate a Management Control Officer to coordinate the efforts of each agency or mission area and to act as a liaison with the Office of the Chief Financial Officer (OCFO).
13. Ensure a prompt response to data and reporting calls issued by the OCFO

.b. On behalf of the Secretary of Agriculture, the OCFO will:

1. Provide oversight to component agencies to ensure that internal and management control programs are established and maintained and that material deficiencies are identified and reported.
2. Establish and maintain systems for monitoring the timely correction of material deficiencies which are reported to the President and Congress.
3. Issue policy guidance and provide technical support to component agencies.
4. Evaluate deficiencies reported by USDA agencies to determine materiality from a Departmental perspective.

5. Prepare and distribute any departmental or external reports of material deficiencies.
6. Keep the Secretary and Sub-Cabinet officials abreast of the status of material deficiencies identified and disclosed.
7. Issue reporting guidelines and data calls, as deemed necessary.

5 OTHER RELATED STATUTES

- a Government Performance and Results Act of 1993, Pub. L. No. 103-62
- b Chief Financial Officers Act of 1990, Pub. L. No. 101-576, as amended
- c Federal Financial Management Improvement Act of 1996, Pub. L. No. 104-208

6. DEFINITIONS

- a Management Controls. The organizational policies and procedures used to reasonably ensure that:
 1. Programs achieve their intended results.
 2. Resources are used consistent with agency and departmental missions.
 3. Programs and resources are protected from waste, fraud, and mismanagement.
 4. Laws and regulations are followed.
 5. Reliable and timely information is obtained, maintained, reported and used for decision making.
- b Management Accountability. Managers are responsible for the quality and timeliness of program performance, increasing productivity, controlling costs and mitigating adverse aspects of agency operations, and assuring that programs are managed with integrity and in compliance with applicable law.
- c Material Deficiency. Encompasses all Section 2 material weaknesses and Section 4 financial management system nonconformances collectively. Judgment must be exercised as to the relative risk and significance of deficiencies. (See APPENDIX A for criteria)

1. Material Weakness. A deficiency or internal/management control weakness in a process that results in a failure to meet one or more of the objectives of Section 2 of FMFIA and that the Secretary of Agriculture determines to be significant enough to report outside the Department.
2. Material Nonconformance. A deficiency or weakness in financial management system operations that results in a failure to meet one or more of the objectives of Section 4 and that the Secretary of Agriculture determines to be significant enough to report outside the Department.

d Reasonable Assurance. A satisfactory level of confidence in achieving program, administrative, and financial management objectives effectively and efficiently and safeguarding government resources under given considerations of costs, benefits, and risks. The emphasis is on the term “reasonable” since “absolute” assurance can never be given for any process.

e Evaluation of Management Control System. A review of program and operational processes and associated management controls to determine compliance with principles, standards and related requirements from the General Accounting Office (GAO), the OMB, or the Joint Financial Management Improvement Program’s “Core Financial System Requirements.” This evaluation may be formal or informal and usually includes an analysis of the general control environment, an analysis of inherent risk and factors external to the agency, and a preliminary evaluation of existing safeguards. The evaluation may be conducted as a separate review or may use the results of existing organizational review processes such as OMB Circular A-130 computer security reviews, OMB Circular A-127 reviews, IG audits and evaluations, GAO evaluations and audits, and other management and consulting reviews. Documentation of results of evaluation must be available for review.

f Risk Assessment. The identification and analysis of possible risks in meeting the agency’s objectives and forming a basis for how these risks should be managed or controlled and the deterrents that should be implemented. The methodology can vary because levels of risk are difficult to quantify. A risk that has little significance and low probability of occurring may require no action at all. However, a risk with high significance and high frequency may require much attention. Assessments should be based on total organization knowledge of the agency program. Appropriate consideration should be given to previous control evaluations such as audit reports, management control reviews, and management evaluations, the degree and timeliness of correcting known material management control weaknesses, and institutional knowledge of the component.

g Internal Controls. A subset of management controls used to assure that there is prevention or timely detection of unauthorized acquisition, use, or disposition of an entity's assets.

APPENDIX A

EVALUATING RISKS AND CRITERIA FOR REPORTING MATERIAL WEAKNESSES AND MATERIAL NONCONFORMANCES

Factors which may assist agency management when evaluating component risks include:

1. **Analysis of the General Control Environment.** The general control environment is management's attitude and discipline concerning controls. An analysis of the general control environment will determine if management's attitude is conducive to a strong and effective control system. The major factors that influence the general control environment are: the presence of a defined organizational structure; the formal delegation of authority; written policies and procedures which reflect current practices; skilled personnel; planning, programming and budgeting for program activity and operations; and reporting and monitoring the execution of planned activity. A subjective analysis of these factors will lead the evaluators to a conclusion on the general control environment.
2. **Analysis of Inherent Risk.** Inherent risk, as defined by OMB Guidelines, is "the inherent potential for waste, loss, unauthorized use, or misappropriation due to the nature of an activity itself." The major factors that affect the inherent risk of an activity within a component are: size of budget, life of component, component administration, nature of component activities, component's impact outside the Department, and special concerns. Inherent risk is outside the control of management and usually stems from factors external to the agency, such as those identified in the strategic planning process. The purpose of assessing inherent risk is to gain an indication of the degree of risk in component operations so that managers can relate the risks involved to control objectives, techniques, and safeguards used and to the frequency of evaluations or risk assessments.
3. **Preliminary Evaluation of Safeguards.** The existence and adequacy of a component's management control system must be evaluated by agency officials exercising professional judgement based on their knowledge and experience with the programs, processes, and operations

within the component. Some questions to consider are whether employee control duties are properly segregated; whether expenditures or other uses of resources are properly authorized; whether funds, property or other resources are adequately protected; whether management monitors controls and provides oversight to identify exceptions from normal program operations; whether there is an active quality review staff to assure periodically that controls are functioning as intended; and whether the results of audits or other studies indicate control weaknesses.

A material weakness under Section 2 of the FMFIA generally falls into one or more of the categories below:

1. Merits the attention of the Executive Office of the President and the relevant Congressional oversight committees.
2. Violates statutory or regulatory requirements.
3. Deprives the public of needed services.
4. Significantly weakens safeguards against waste, loss, unauthorized use or misappropriation of funds, property or other assets.
5. Significantly impairs the fulfillment of the Department or organization mission.
6. Results in a conflict of interest.
7. Is of a nature that omission from the annual FMFIA report could reflect adversely on the actual or perceived management integrity of the Department.

All material weaknesses identified in audit reports are to be “considered” for inclusion in the Integrity Report. However, OMB’s definition of “material weakness” should not be confused with use of the same term by government auditors to identify management control weaknesses which, in their opinion, pose a risk or a threat to the internal control systems of an audited entity, such as a program or operation. Auditors are required to identify and report those types of weaknesses at any level of operation or organization, even if the management of the audited entity would not report the weaknesses outside the agency.

A material nonconformance under Section 4 generally falls into one or more of the categories below:

1. Merits the attention of the Executive Office of the President and the relevant Congressional oversight committees.
2. Prevents USDA primary accounting systems from achieving central control over agency financial transactions and resource balances.
3. Prevents compliance of the primary accounting system with standards published by GAO, which include the availability of timely, consistent, and relevant financial information for decision-making purposes.